

## IBC16's Easy Explainers



### Infrastructure Leasing and Financial Services Limited

#### The Background

IL&FS is a non-banking financial company ("NBFC"), which was established over 30 years ago. It was founded by three financial institutions, namely the Central Bank of India, Housing Development Finance Corporation, and Unit Trust of India, to fund major infrastructure projects. It is used to fund the projects of the financial and development sectors such as tunnels, roads, metro, etc.



## The Origin of Troubles

- The IL&FS crisis started when some of its subsidiaries could not pay back the loans and inter-corporate deposits. The IL&FS Transportation Networks (“ITNL”) delayed the repayment of Rs. 450 crores of ICD from the Small Industries Development Bank of India (“SIDBI”).
- Further, IL&FS group defaulted in the payment of Rs. 1000 crores in the short-term loan taken from SIDBI. Even with no new infrastructure projects, the running projects of IL&FS faced cost overruns and it also failed to meet its commercial paper redemption obligations.
- Subsequently, credit rating agencies such as ICRA and Brickwork Ratings downgraded their rating of its borrowing programmes, thereby affecting the position of investors and lending institutions.

## Timeline of the case

- **Application by the Central Government under Section 241 & 242 of the Companies Act, 2013 (“the Act”)** (1 October 2018)

After IL&FS faced difficulty in repaying its debts, the Central Government filed an application under Sections 241(2) & 242 of the Companies Act, 2013 (Application to Tribunal for relief in cases of oppression, etc.) before the NCLT, Mumbai Bench. The government sought immediate suspension of the existing board of directors of IL&FS and appointment of a new board, on the ground that the affairs of IL&FS holding company and its group companies were being conducted in a manner prejudicial to the public interest. Also, the government sought the appointment of 10 persons as directors in terms of Section 242(2)(k) of the Act, to manage the affairs of IL&FS.

- **Suspension of the existing board of directors and appointment of a new board** (1 October 2018; NCLT, Mumbai Bench)

Vide its order dated 1 October 2018, NCLT, invoking the powers conferred upon it under Sections 242 & 246 of the Act, suspended the existing board of directors with immediate effect and constituted a new board consisting of six directors (as was proposed by the government through an Additional Affidavit). Liberty was granted to the new board to select a new Chairman from amongst themselves. Mr. Uday Kotak was appointed as the chairman. Also, the tribunal directed the new board to prepare a roadmap for the resolution of IL&FS and its group companies.

- **Grant of immunity to the newly appointed directors** (5 October 2018; NCLT, Mumbai Bench)

An application was filed by the government seeking specific immunity to the newly appointed directors, to ensure independent functioning of the said directors individually and collectively. Due to the default of IL&FS, the directors may become subject to disability or disqualification under the law including, but not limited to, Sections 164 & 167 of the Act. Therefore, NCLT, vide its [order dated 5 October 2018](#), issued directions that for the past actions of the suspended directors or any of the officers of IL&FS, no action should be initiated against the newly appointed directors, without prior approval of the tribunal.

- **Application for moratorium rejected by the NCLT** (12 October 2018; NCLT, Mumbai Bench)

An application was filed by the government seeking a comprehensive moratorium qua IL&FS and its group companies as they might be subject to several creditor actions, which would hinder the resolution process. The government contended that in order to ensure fair resolution of the company, the status quo needs to be preserved with respect to the business. The Tribunal rejected the prayer for issuing a moratorium vide its [order dated 12 October 2018](#).

- **NCLAT coming to the rescue** (15 October 2018)

The government preferred an appeal to the NCLAT against NCLT's rejection. NCLAT, vide its [order dated 15 October 2018](#), granted moratorium (until further orders) qua IL&FS and its group companies, taking into consideration the nature of the case, larger public interest and economy of the nation.

- **Impleadment of additional respondents in the original petition** (3 December 2018; NCLT, Mumbai Bench)

The government filed an application before the NCLT seeking impleadment of certain persons as party respondents in the original petition. The application was based on the findings of the Serious Fraud Investigation Office ("SFIO") in their interim report, which revealed numerous instances of dubious transactions, conflict of interest, misreporting of income, and personal enrichment of key employees of the company.

NCLT, vide its [order dated 3 December 2018](#), allowed the application saying that the proposed respondents were holding the key managerial positions for more than 20-25 years in different capacities in IL&FS and its group companies, and their impleadment as respondents in the case is necessary to render a complete and effective adjudication. Further directions were issued against the additional respondents, restraining them from mortgaging or creating charge or lien or creating third party interest or in any way alienating, the movable or immovable properties owned by them, including jointly held properties.

- **Suo Motu interjection by the Institute of Chartered Accountants of India (“ICAI”)**

With news spreading across the market regarding the diversion of loan money in IL&FS and its subsidiary companies, the Disciplinary Directorate of ICAI had suo motu [taken cognizance](#) of the matter. They issued notices to the audit firms that carried out audit works of IL&FS for the last 5 years.

Through an inquiry conducted by ICAI, it [found that](#) the statutory auditors of IL&FS were prima facie guilty of professional misconduct and there were lapses and manipulations in the financial statements by the auditors.

- **Re-opening of books of accounts of IL&FS** (1 January 2019; NCLT, Mumbai Bench)

Pursuant to the reports and findings of SFIO and ICAI, the government filed a petition before the NCLT under Section 130 of the Act (Re-opening of accounts on court's or tribunal's orders), seeking re-opening of IL&FS and its group companies for the past five financial years i.e. from Financial Year 2012-2013 to Financial Year 2017-2018. They also sought the appointment of a person/firm of chartered accountants to recast the accounts/financial statement of the said companies.

NCLT, vide its [order dated 1 January 2019](#), allowed the petition and directed the government to appoint a person/firm as the chartered accountants to recast the accounts/financial statement of the said companies.

- **Government submits resolution plan for IL&FS** (4 February 2019)

On 4 February 2019, the government submitted the debt resolution plan for IL&FS to the NCLAT and also suggested the name of a retired Supreme Court judge, Justice DK Jain, to supervise the entire process. The entire resolution process was to be based on the principles enunciated in the Insolvency and Bankruptcy Code 2016 ("the Code"). Under the plan, the government had categorized IL&FS Group companies into green (entities that have enough money to service all their debts), amber (entities that could pay the secured creditors, but not the unsecured ones), and red (entities not in a position to pay any creditor), based on their respective financial positions.

- **Appointment of Justice DK Jain to supervise the resolution process** (11 February 2019, NCLAT, New Delhi Bench)

NCLAT, vide its [order dated 11 February 2019](#), approved the appointment of Justice DK Jain to supervise the resolution process of IL&FS and its group companies. Also, the tribunal allowed 22 companies of the IL&FS Group, which were classified in the 'green' category based on their financial health, to service their debt obligations.

- **Raids by the Enforcement Directorate ("ED")** (20 February 2019)

On 20 February 2019, ED conducted raids on at least six locations in Mumbai and Delhi-NCR, in connection with the IL&FS default crisis. The action by ED came after it registered a criminal complaint under the Prevention of Money Laundering Act ("PMLA") in the IL&FS case. ED had registered the case on the basis of a separate FIR registered by Delhi Police's Economic Offence Wing ("EOW") for allegations related to cheating and forgery against the IL&FS group and its managing committee that took place between 2010 and 2018.

- **No declaration of accounts of IL&FS or its group companies as Non-Performing Assets ("NPA"), without prior permission of NCLAT** (25 February 2019; NCLAT, New Delhi Bench)

NCLAT, vide its [order dated 25 February 2019](#), cleared that due to non-payment of dues by the IL&FS or its group companies, no financial institution will declare the accounts of the said companies as 'NPA' without prior permission of this tribunal.

- **Stay by the Supreme Court on re-opening books of accounts of IL&FS** (29 April 2019; Supreme Court)

An appeal was preferred before NCLAT against the NCLT's order of re-opening of books of accounts of IL&FS. NCLAT, vide its order dated 31 January 2019, dismissed the said appeal. A further appeal was preferred before Supreme Court. The Apex Court, vide its [order dated 29 April 2019](#), declared a stay on the operation of NCLAT's order.

- **Modification of the order dated 25 February 2019** (2 May 2019; NCLAT, New Delhi Bench)

After the order of NCLAT restraining the banks from declaring the loan accounts as NPA, the Reserve Bank of India ("RBI") filed an interlocutory application before this tribunal for vacating the said order. After hearing the contention, the tribunal found that NPA relates to an asset i.e., loan or advance which becomes non-performing when it ceases to generate income for the banks. Thus, the declaration of accounts as "NPA" by the banks will not affect the company to continue as a going concern.

Considering this position of law, NCLAT modified its previous order and allowed the banks to classify loan accounts of IL&FS or its group companies as NPA.



- **SFIO's chargesheet against 30 individuals** (30 May 2019)

SFIO filed its first chargesheet in the IL&FS case against 30 individuals and entities, including the auditor firms of the company. They accused auditors Deloitte Haskins & Sells ("DHS") LLP and BSR & Co LLP of concealing information and falsifying accounts.

- **Ministry of Corporate Affairs ("MCA") moves against the auditors under Section 140(5) of the Act** (1 June 2019)

[MCA moved](#) NCLT under Section 140(5) of the Act for debarment of the audit firms and their audit partners for their role in perpetuating the fraud at a subsidiary of IL&FS. They also sought attachment of the properties of the auditors, including bank accounts and lockers.

- **Supreme Court puts to rest the issue of re-opening the books of accounts** (4 June 2019; Supreme Court)

After much debate, Supreme Court, vide its [order dated 4 June 2019](#), allowed and confirmed the re-opening of the accounts and re-casting the financial statements of IL&FS and its group companies for the past five financial years.

- **ED arrests two former Executives of IL&FS (19 June 2019)**

On 19 June 2019, ED arrested Arun Saha, the former Joint Managing Director of IL&FS, and K Ramchand, former Managing Director of the company's subsidiary ITNL, in PMLA probe, marking its first arrest in the IL&FS case.

- **NCLT, vide its [order dated 18 July 2019](#), allowed the impleadment of certain independent directors and auditors as party respondents in the original petition (18 July 2019; NCLT, Mumbai bench)**
- **Approval of the resolution framework by NCLAT (12 March 2020; NCLAT, New Delhi Bench)**

[On 12 March 2020](#), NCLAT allowed for restructuring of IL&FS and its entities by approving the resolution framework proposed by the government, which demanded that there should be fair and equitable distribution of funds to all the creditors. However, NCLAT refused to follow the waterfall mechanism for distribution of proceeds, as laid down under Section 53 of the Code, citing the reason that public money is involved in the process and all the creditors must be equally treated.